

September 28, 2009

Summary:

Newport Beach Assessment District No. 103, California; Miscellaneous Tax

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Summary:

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Credit Profile

US\$3.335 mil 2009 Lmt'd Ob Improv bnds due 09/02/2024

Long Term Rating

A/Stable

New

Rationale

Standard & Poor's Ratings Services assigned its 'A' rating to Newport Beach Assessment District No. 103, Calif.'s series 2009 limited-obligation improvement bonds. The rating reflects our view of:

- A built-out, wealthy residential district, with the vast majority of parcels made up of owner-occupied homes;
- Relatively modest assessments given the district's average assessed value (AV), with effective tax rates at 1.2% of AV for the average AV in the district; and
- A strong overall value-to-lien ratio of 36 to 1, including overlapping debt.

Tempering factors include our view of the district's:

- Relatively small debt service reserve fund funded at 6% of principal; and
- Inability to increase assessment rates, a factor in all similar ratings.

A pledge of special assessments owed by parcel owners within Assessment District No. 103 secures the bonds. Pursuant to the Improvement Bond Act of 1915, annual assessments are liens on assessed parcels to provide 1x coverage of the bonds issued to finance the removal of above-ground utility poles and wires and relocating them underground.

Assessment District No. 103 is located at the tip of the Balboa Peninsula in Newport Beach. Surrounded by water on three sides and just blocks from the beach, it is a mature area with high-end homes. Assessment District No. 103 is entirely residential and covers 26 acres. There are 211 parcels with assessments that secure the bonds. Single-family homes account for 88% of assessments (189 parcels). Multifamily residential (17 parcels and 10% of assessments), condominiums (3 parcels and 1% of assessments), and vacant land (2 parcels and 1% of assessments) make up the remainder.

The district has been built out for decades. Most of the new construction involves remodeling smaller, older houses into larger houses. Property turnover has been, in our view, relatively low in recent years; based on these transactions, median homes prices are more than \$3 million. The direct and overlapping value-to-lien ratio is 36 to 1 based on 2010 AV, and a higher 51 to 1 on a direct-debt basis. AV for the entire district was \$169 million in fiscal 2010. This was a decrease of 4.7% in fiscal 2009 AV, a result of countywide action taken by the assessor to preemptively address value through Proposition 8 reductions as a result of the recent housing run-up. The average fiscal 2010 AV for the district is \$799,000, still well below recent home sales.

Annual assessments on parcels are what we consider small compared with the AV of property within the district; a

typical annual residential assessment of \$1,364 in the district accounts for roughly 0.17% of average AV in the district. Including this assessment, other smaller per-parcel taxes, and ad valorem taxes, the effective tax rate for homes in the district is, in our view, low (1.2% for the average AV of the district in fiscal 2010 and 1.1% for a sample \$2.3 million home). Delinquent property taxes in district No. 103 have been historically what we consider low. Based on current data for most of September 2009, the district had a 1.8% delinquency rate for fiscal 2009.

The project area is, in our view, diverse, with the 10 taxpayers making up only 12% of the assessments. The largest taxpayer, an individual homeowner, makes up only 1.5% of the assessments (and 1.1% of fiscal 2010 AV). None of the top 10 taxpayers owns more than two parcels.

The bonds mature in 2024. The reserve requirement is the least of maximum annual debt service, 125% of average annual debt service, or 6% of original principal. In practice, the 6% of original principal is the functional debt service reserve amount given that this is significantly lower than the other two requirements. We believe that the reserve, at 6% of principal, provides enough financial cushion so the district can sustain the loss of 4.3% of assessments annually for the bonds' life without needing to foreclose on delinquent properties by drawing on the reserve since the district cannot increase assessments. This is a closed lien, and the district cannot issue additional parity bonds except for refunding bonds.

The City of Newport Beach is a wealthy, mature coastal city located in a central portion of the Orange County coast. Income levels, as measured by effective buying income, are, in our opinion, very strong on a household and per capita basis at 191% and 283% of the nation, respectively. Unemployment in Newport Beach was 6.1% in August 2009 (not seasonally adjusted), below the state rate of 12.1% and the national rate of 9.7%.

Outlook

The stable outlook reflects our expectation that the diversity of individual homeowners as taxpayers will provide stability in the payment of the assessments. Additionally, the outlook reflects our expectation that the assessment district will retain strong property values and that further delinquencies will remain minimal.

Related Research

USPF Criteria: "Special-Purpose Districts," June 14, 2007

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